Office-Supreme Court, U.S.
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No. 258

IN THE

United States Court of Appeals

FOR THE THIRD CIRCUIT

AMERICAN WELL AND PROSPECTING COMPANY,
Petitioner,
—*against*—
COMMISSIONER OF INTERNAL REVENUE,
Respondent.
No. 11,588

PETITION FOR REHEARING

To the Honorable, the Judges of the United States Court of Appeals for the Third Circuit:

Now comes the petitioner, by its counsel, and respectfully prays this Court that this case be reheard and reconsidered, for the following reasons:

1. *This Court held that the taxpayer was de facto dissolved on January 2, 1946, because (i) there was no business purpose for its continued existence and (ii) it was kept alive for tax evasion purposes, whereas*

(a) *the Tax Court found that the taxpayer remained in existence for a proper business purpose;*

(b) *the Tax Court's finding not only was supported by substantial evidence, but also was undisputed and*

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adopted by the Commissioner in his brief in phrasing the question presented by the appeal;

(c) *the Commissioner has not contended that the taxpayer was kept alive to avoid tax; and*

(d) *there was in fact no avoidance of tax.*

2. *Since the taxpayer was continued in existence for a proper business purpose and since there was no tax avoidance, the decision of the Tax Court which is based on a ground repudiated by this Court and other Courts of Appeals, should be reversed.*

I.

THIS COURT DECIDED THE CASE ON A GROUND WHICH IS CONTRARY TO A FINDING OF FACT BY THE TAX COURT THAT WAS BASED ON SUBSTANTIAL EVIDENCE.

The taxpayer on January 2, 1946, *sold* all its *assignable* assets to Bethlehem Supply Company (Supply), a corporation which was engaged in the same type of business as the taxpayer (13a). The taxpayer agreed to collect some $300,000 in *unassignable* claims against the United States which had arisen in its business and, when it had finished collecting them, to transfer the proceeds thereof to Supply. This problem of collecting non-assignable claims does not arise where the business assets are transferred to a stockholder in liquidation (*Novo Trading Corporation* v. *Commissioner*, 113 F. 2d 320 (2nd Cir. 1940)) but does arise on a sale to a third party (*United States* v. *Shannon*, 342 U. S. 288 (1952)). If the taxpayer had sold those claims to Supply on January 2, 1946, they would have become

void.* The taxpayer had not finished collecting such unassignable claims by the end of 1946 (13a, 16a, 17a, 24a).

This Court's decision that the taxpayer was not entitled to an excess profits credit for the calendar year 1946 is predicated upon its finding that the taxpayer was *de facto* dissolved on January 2, 1946, when it transferred all its *assignable* assets** to Supply, because (1) the taxpayer was kept alive "only for purposes of tax evasion" (p. 8 of the opinion), and (2) there was no business reason after that date for continuing the taxpayer's existence (p. 9 of the opinion).

The Tax Court found, however, that the taxpayer

> "remained in existence to cooperate with the purchaser [of its assets] so that the latter might derive the benefit of certain contracts and claims that were unassignable" (3a).***

That undisputed finding of the Tax Court is in direct conflict with this Court's finding of *de facto* dissolution because there was no business reason for continuing the taxpayer's existence.

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*The relevant part of 10 Stat. 170, as amended, Section 203, Title 31, United States Code reads as follows:

> "All transfers and assignments made of any claim upon the United States, or of any part or share thereof, or interest therein, whether absolute or conditional, and whatever may be the consideration therefor, and all powers of attorney, orders, or other authorities for receiving payment of any such claim, or of any part or share, thereof, shall be absolutely null and void, unless they are freely made and executed in the presence of at least two attesting witnesses, after the allowance of such a claim, the ascertainment of the amount due, and the issuing of a warrant for the payment thereof. * * *"

**This Court correctly states that the taxpayer transferred only its assignable assets (p. 2), but later (p. 8) when finding that there was no business purpose for the taxpayer's continued existence, incorrectly states that Supply "had acquired all the taxpayer's assets".

***Headnotes of Tax Court opinions are prepared by the Court and are considered to be a part of the Findings of Fact and Opinion

The Commissioner, far from contesting the Tax Court's finding, accepted it in his brief and incorporated it in his statement of the question presented by the appeal, stating that the taxpayer

> "remained in existence to cooperate with the purchaser so that the latter might derive the benefit of certain contracts and claims that were unassignable" (Br., p. 2).

The Tax Court's finding of fact that the taxpayer remained in existence for the business purpose of cooperating with the purchaser of its assets in connection with the collection of unassignable claims is supported by substantial evidence. The Tax Court found that the taxpayer had claims against the United States, which arose out of the business it had formerly conducted, in the amount of approximately $300,000 (6a). Those claims were not assigned by the taxpayer on January 2, 1946. They were nonassignable because of the provisions of 10 Stat. 170, as amended, Section 203, Title 31, United States Code, *supra*. If the taxpayer had sold them to Supply on January 2, 1946, they would have become *void*. *United States* v. *Shannon*, 342 U. S. 288 (1952), *supra*.

Accordingly, it was necessary that the taxpayer remain in existence in order to collect those claims and complete its agreement by transmitting the proceeds of the claims to Supply, the purchaser of its assets. We submit that it is a misstatement of law to say that the taxpayer collected those claims as agent for Supply, as stated in this Court's opinion (p. 7). Supply had no right to collect the claims and its agent could have no greater right than the principal. It was essential that the taxpayer collect those unassignable claims *in its own right*. It is stipulated that the taxpayer

acted through its officers (who were also officers of Supply) in collecting the claims (7a). If there was any agency involved it was the other way around, i.e., Supply acted as agent for the taxpayer in collecting the claims.

The crux of this Court's holding is contained in the following two sentences in its opinion (p. 9):

> "In any event, there could be only two reasons for keeping a corporation alive under the circumstances of the case at bar in 1946: to avoid taxes, or to have a spare corporate charter conveniently ready for use whenever desired by the parent corporation. Neither is a sufficient business purpose of the taxpayer to negate the Tax Court's finding that the taxpayer in the case at bar was not entitled to an unused excess profits credit carry-back from the tax year 1946."

But the Tax Court had already made an undisputed finding as to the business reason for continuing the taxpayer's existence, namely, so that the purchaser of its assets might derive the benefit of unassignable claims. We do not see how the above quotation from this Court's opinion setting forth two wholly different reasons (neither of which appears to us to find support in the record) can stand in the light of the Tax Court's finding of fact that there was a business purpose for continuing the taxpayer's existence.

That the $300,000 of non-assignable claims were not shown on the taxpayer's balance sheet after January 2, 1946, is not of any importance, because good accounting practice would not permit such claims to be shown as an asset unless a like amount were set up as a liability on the other side of the balance sheet. It is stipulated that the taxpayer owned them and did not collect any of them until

May, 1946 (15a) and that some $25,000 remained uncollected at December 31, 1946 (16a).

Surely, the collection of non-assignable claims arising out of its business which it owned and which only it could collect was a part of the orderly winding up of a taxpayer's affairs which this Court has held to be proper corporate business. *Commissioner* v. *Wayne Coal Mining Company*, 209 F. 2d 152 (3rd Cir. 1954). The collection of accounts receivable has always been considered a proper reason to delay dissolution. Admittedly, counsel for the taxpayer could not properly have advised that the taxpayer be dissolved prior to the collection of the non-assignable claims against the United States nor, indeed, was such dissolution advisable until the termination in 1948 of a pending suit against the taxpayer for $219,000 (7a). By that time, the taxpayer was actively engaged in another business (8a).

This Court's opinion indicates that it was under the misapprehension that the Tax Court had found that the taxpayer was *de facto* dissolved on January 2, 1946, and that it was merely affirming that finding. On the contrary, as pointed out above, the Tax Court found that there was a proper business purpose for continuing the taxpayer's existence, as indeed there was, in order to avoid forfeiture of the unassignable claims.

The Tax Court did not find that the taxpayer was *de facto* dissolved in 1946. When the Tax Court in this type of case makes a finding of *de facto* dissolution, it does so in unequivocal language. For instance, in *A B C Brewing Corp.*, 20 T. C. 515 (1953), the Tax Court found (p. 527):

> "On the facts in the instant case, we think that the petitioner must be held to have been de facto dissolved at the beginning of the fiscal year 1945 and, consequently, not entitled to a carry-back of excess profits credit from that year or from 1946."

The United States Court of Appeals for the Ninth Circuit refused to reverse that finding of fact because it was supported by substantial evidence (224 F. 2d 483 (9th Cir. 1955)). Hence in the instant case, this Court may not properly reverse the finding of fact that the taxpayer's existence was continued for a proper business purpose.

There was in Fact No Avoidance of Tax

This Court's implication that the taxpayer was "kept alive only for purposes of tax evasion" (p. 8) and its statement that the taxpayer was kept alive "to avoid taxes" (p. 9), are, as pointed out above, not only contrary to the Tax Court's finding of fact, but do not have any support in the record.

The Commissioner has never urged that the taxpayer was kept alive for purposes of tax evasion or avoidance. On the contrary, the Commissioner has admitted that any "abuse" of the carry-back provisions by the taxpayer would have been "unintentional" (Br., p. 12).

Since the Commissioner did not take the position that the taxpayer's existence was continued for tax evasion purposes, it was not part of the taxpayer's burden of proof to counteract a non-existent charge. We believe that, in fairness, the taxpayer should be permitted to present facts to rebut a charge of tax evasion now made for the first time.

The fact is that *no tax was avoided by the sale of the taxpayer's business to Supply.*

The taxpayer lost money in 1945 (Exhibit 3-C). If the taxpayer's business in the hands of Supply also lost money in 1946 (which we believe to be the case), then the taxpayer would have been entitled to the same unused excess profits credit carry-back for 1946 it is now claiming,

plus an operating loss carry-back, if it had not sold its business to Supply on January 2, 1946. Accordingly, the Treasury would not have collected any more tax from the taxpayer if it had retained its business for all of 1946 (instead of selling it on January 2, 1946) than the Treasury would collect if the instant case were decided in the taxpayer's favor.

On the other hand, if (contrary to what we believe to be true) the former business of the taxpayer produced net income in 1946 in the hands of Supply, there was still no tax advantage to the Bethlehem group by reason of the transfer of the business to Supply, and hence there could be no tax evasion motive.

Supply's operations in 1946, taking into account any 1946 income from the business of the taxpayer, resulted in a net loss for 1946. Hence Supply had an unused excess profits credit carry-back and a net operating loss carry-back from 1946 to 1944 and 1945 which resulted in a refund of part of the excess profits tax which it paid in those years. Any 1946 income from the assets which the taxpayer transferred to Supply merely reduced the carry-back of Supply (instead of the carry-back of the taxpayer) and at least correspondingly reduced Supply's refund of excess profits tax. *Accordingly, the excess profits tax collected by the Treasury would have been no less had the taxpayer operated its business for all of 1946, instead of selling it to Supply.* Any lessening of the taxpayer's carry-back by any income from that business which would have occurred had the taxpayer retained it during 1946 was compensated for by a decreased carry-back to Supply, the new owner of the business. Thus on the assumption that the taxpayer's assets produced income in 1946, this Court's decision, instead of preventing a supposed tax *advantage* arising from

the sale of the taxpayer's assets (as this Court apparently thought it was doing), actually *penalizes* a transaction which could not result in decreasing the excess profits tax collected by the Treasury.*

Since there was no avoidance of tax, the continued existence of the taxpayer could not possibly have been, as stated by this Court, "only for purposes of tax evasion" (p. 8), or "to avoid taxes" (p. 9). Those references should, therefore, be eliminated from this Court's opinion.

II.

SINCE THE TAXPAYER WAS CONTINUED IN EXISTENCE FOR A PROPER BUSINESS PURPOSE AND SINCE THERE WAS NO TAX AVOIDANCE, THE DECISION OF THE TAX COURT, WHICH IS BASED ON A GROUND REPUDIATED BY THIS COURT AND OTHER COURTS OF APPEALS, SHOULD BE REVERSED.

We believe it will be apparent to this Court that since the taxpayer was continued in existence for a proper business purpose and since there was no tax evasion or avoidance, the decision of the Tax Court must be reversed. That is true even though, as stated on p. 6 of this Court's opinion, the question is considered on the assumption that the taxpayer had "eventually been liquidated without acquiring any additional operating assets".

On the basis of what we believe to be controlling authority, corporations which are continued in existence to collect accounts receivable after they have disposed of their assets preparatory to liquidating are entitled to an excess profits credit under the mandatory wording of Section 710 of the

*The facts contained in this paragraph are not in the record as no charge of tax evasion or avoidance has previously been made.

Internal Revenue Code of 1939, where they are not kept alive merely for tax evasion purposes. *Commissioner* v. *Allegheny Broadcasting Corporation*, 179 F. 2d 844 (3rd Cir. 1950); *Wier Long Leaf Lumber Co.* v. *Commissioner*, 173 F. 2d 549 (5th Cir. 1949) [as to the tax year 1943]; *Bowman* v. *Glenn*, 84 F. Supp. 200 (W. D. Ky. 1949), affirmed 184 F. 2d 670 (6th Cir. 1950); *United States* v. *Kingman*, 170 F. 2d 408 (5th Cir. 1948).

With the finding of a proper business purpose for the continued existence of the taxpayer, and absent any tax evasion or tax avoidance, the language of this Court in the *Allegheny Broadcasting Corporation* case, *supra*, is particularly relevant (p. 848 of 179 F. 2d):

> "We do not have here a case in which the corporate existence was continued solely for the purpose of avoiding taxation for the Tax Court has found that the dissolution of KQV was deferred for adequate reasons. Accordingly we are not called upon to consider the case upon the theory that it discloses an attempt to evade the intent of the act."

It appears to us that the opinion of this Court, if unchanged, would overrule *sub silencio* the decision of this Court in the *Allegheny Broadcasting Corporation* case,* *supra*, in which this Court refused to hold that a corporation was dissolved *de facto* during the calendar year 1945 even though it had adopted a resolution of liquidation and dissolution, transferred *all its assets* (p. 554 of 12 T. C.) to its stockholders (who assumed its liabilities) in liquidation on February 28, 1945, and thereafter ceased to do business. The only activities in which the corporation there involved was engaged after February 28, 1945, were (1)

*Decided by a division of this Court which did not include the writer of the opinion in the instant case.

to determine its Pennsylvania unemployment compensation tax liability in the amount of less than $1,000 and (*2*) to file an application for excess profits tax relief under Section 722 of the Internal Revenue Code of 1939 with respect to the calendar year 1945. There, this Court accepted the Tax Court's finding that such activities constituted adequate reasons for delaying the formal dissolution of the corporation and refused to hold that the corporation was *de facto* dissolved at any time during the year 1945, even though it was formally dissolved as early as February 28, 1946. This Court cites the *Allegheny Broadcasting* case in footnote 8 on p. 7 of its opinion under the heading: "Cases where courts have found sufficient business activity to entitle corporations in liquidation to excess profits credits".

Since the taxpayer, on the authority of the cases above cited, would have been entitled to an excess profits credit and an unused excess profits credit carry-back from the taxable year 1946 even had it "eventually been liquidated without acquiring any additional operating assets", we believe that this Court must agree that the facts that the petitioner never passed a resolution of liquidation, never made any liquidating distributions and never showed any intention to liquidate or dissolve do not provide reasons for denying it the credit carry-back.

The importance of the retention by the taxpayer of its assets is that it did not, as did the corporations in *Winter & Company, Inc. (Indiana)*, 13 T. C. 108 (1949), and *Wheeler Insulated Wire Co.*, 22 T. C. 380 (1954) (relied upon by this Court in its opinion (p. 8)), destroy "its potentiality for the production of income by disposing of its capital", to quote the Tax Court in the *Winter* case, *supra* (p. 115 of 13 T. C.). If the taxpayer was a "shell" as

stated by this Court (p. 8), it was a shell that still retained its kernel. We submit that the real significance of the fact that the taxpayer used its retained capital to purchase another business in 1948 is that it shows that there was never any *intention* to liquidate or dissolve.

The crux of the Tax Court's decision in the instant case is shown by the following quotation from its opinion (9a, 10a):

> "The petitioner, at the beginning of 1946, disposed of the assets essential to the continued operation of the business which it had conducted with those or similar assets in 1944. Those assets were used during 1946 by Supply to carry on the business theretofore conducted by the petitioner. The results of the operation of that business during 1946 had no effect upon the petitioner but there might have been no excess profits credit to carry back to 1944 had the petitioner continued to conduct the business during 1946. Where the business was thus transferred to another and no longer operated by the petitioner, the latter was not intended by Congress to have the excess profits credit, wholly unnecessary for 1946, carried back to offset income of a year when the petitioner had operated the business."

In so holding, the Tax Court was merely following its own decision in *Wier Long Leaf Lumber Co.*, 9 T. C. 990 (1947), as to the year 1943, in which case the taxpayer had sold its business to a third party on December 24, 1942, but was engaged in 1943 in collecting its accounts receivable. The United States Court of Appeals for the Fifth Circuit reversed (173 F. 2d 549, *supra*), saying:

> "The fact of which the Commissioner makes so much, that before the end of 1942, the corporation had sold its mill and was no longer making

> money as an active sawmill company seems to us to be without significance here. * * * Finally, it is not claimed, it could not be, that the liquidation was entered upon here with any tax advantage purpose in mind. For it is clear from this record that the liquidation could not, and did not, confer any tax advantage."

Accordingly, the opinion of this Court, if unchanged, stands alone in holding that a corporation which after it sold its assets was engaged in collecting unassignable claims, which never passed a resolution of liquidation, which never made any liquidating distributions, which did not have any intention of liquidating or dissolving and which was not kept alive for tax avoidance purposes has somehow become *de facto* dissolved. We believe that such a decision is so far reaching in its implications as to deserve a rehearing and reconsideration by this Court.

Conclusion

In view of the fact that this Court apparently decided the case on a misunderstanding of the facts as to (i) the business purpose for the taxpayer's continued existence, and (ii) whether or not any tax had been avoided by the sale of the taxpayer's assets on January 2, 1946, this Court should grant a rehearing and set a date for reargument.

Respectfully submitted,

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Certificate of Counsel

I, GEORGE G. TYLER, counsel for the above-named petitioner, do hereby certify that the foregoing Petition for Rehearing is presented in good faith and not for delay.

GEORGE G. TYLER

April 4, 1956.

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In the Supreme Court of the United States

OCTOBER TERM, 1956

AMERICAN WELL AND PROSPECTING COMPANY,
PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 232 F. 2d 934. (Pet. Ex. A.) The opinion of the Tax Court (R. 3a–10a) [1] is reported at 23 T. C. 503.

JURISDICTION

The judgment of the Court of Appeals was entered on March 22, 1956 (Pet. Ex. B), and a petition for rehearing was denied on April 18, 1956 (Pet. Ex. C). The petition for certiorari was filed on July 17, 1956. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

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[1] Record references are to the appendix to the taxpayer's brief in the Court of Appeals.

QUESTION PRESENTED

The taxpayer corporation disposed of all of its assets and ceased operating its business as of December 31, 1945, but remained in existence during 1946 to cooperate with the purchaser of its assets so that the latter might derive the benefit of certain unassignable contracts and claims. The question presented is whether the taxpayer, on these facts, is entitled to carry-back an unused excess-profits credit for 1946 to 1944 under Section 710 of the Internal Revenue Code of 1939.

STATUTE AND REGULATIONS INVOLVED

Section 710 (a) (1), (b) (2) and (3), (c) (1), (2), and (3) (A) of the Internal Revenue Code of 1939, and Sections 35.710–1, 35.710–2, and 35.710–3 of Treasury Regulations 112, are set forth in the Appendix, *infra*, pages 15–20.

STATEMENT

The pertinent facts, as stipulated (R. 12a–18a) and as found by the Tax Court (R. 3a–8a), may be summarized as follows:

The taxpayer, a Texas corporation, was organized in 1931. For a number of years prior to 1946, the taxpayer was engaged in the business of manufacturing and selling oil-well rotary-drilling equipment and accessories and of manufacturing armaments for the United States Government. Bethlehem Steel Company, at all times material hereto a wholly owned subsidiary of Bethlehem Steel Corporation, acquired all of the outstanding stock of the taxpayer in 1944 and has since continued to own that stock. On December 19, 1945, the taxpayer entered into a contract with

Bethlehem Supply Company, hereinafter referred to as Supply, for the sale of all of its transferable assets and assumption of all of its transferable obligations and liabilities as of the opening of business on January 1, 1946. Supply was then and still is a wholly owned subsidiary of Bethlehem Steel Corporation. (R. 4a.)

The taxpayer agreed to sell to Supply all of its real property, machinery, equipment, raw materials, goods in process or completed, contracts and leases, patents, trademarks and trade names, cash and receivables, and all other property except certain unassignable rights and interests. The contract of sale also excluded the taxpayer's corporate records and franchise and certain equipment physically located in its plant but owned by the United States Government or agencies thereof. Supply agreed to assume, pay, perform, or discharge all of the liabilities and obligations of the taxpayer as of the opening of business on January 1, 1946, and further agreed to perform for the account of the taxpayer all obligations of the taxpayer with respect to certain contracts and leases relating to machinery and equipment owned by the United States Government and located at the taxpayer's plant. It was agreed that if the taxpayer subsequently purchased any such equipment it would, unless prohibited by its agreement with the Government, resell the same to Supply at cost. (R. 4a–5a.)

The contract further provided that as soon after the closing date as conveniently possible Supply would pay to the taxpayer for the properties to be sold an amount which would be the aggregate net book value

of such properties less the aggregate book value of all the liabilities and obligations of the taxpayer assumed by Supply. The taxpayer also agreed that, in the event any of the rights or interests or any of the obligations under any of its contracts were not assignable to Supply, it would seek to obtain any consents necessary to permit such assignments. The taxpayer was required to cooperate with Supply, if such consents could not be obtained, to the end that the obligations of the taxpayer should "be performed in such manner that the value and benefits of the contract in question shall be preserved and shall inure directly or indirectly to the benefit of the Supply Company." (R. 5a.)

The contract was closed on January 2, 1946, by the delivery of instruments of conveyance dated December 31, 1945, and by assumption by Supply of all liabilities and obligations of the taxpayer as of the opening of business on January 1, 1946. (R. 5a.)

Among the assets owned by the taxpayer and which were covered by the agreement were certain claims against the United States Government which were ~~opening of business on January 1,~~ largely settled ... 1946. (R. 5a.)

The taxpayer had correspondence in 1946 and 1947 with various United States Government departments with respect to clean-up work which it was obligated to do under the terms of contracts executed in prior years. The taxpayer purchased from the United States, in connection with this work, certain material and machinery owned by the Government but located on the property formerly owned by the taxpayer. The amounts necessary for such purchases were furnished

by Supply and the proceeds of the sales of such material and machinery were realized by Supply. The taxpayer, in October, 1951, settled for approximately $1,300 a claim asserted against it by the United States Government for defective material delivered prior to January 1, 1946. The settlement negotiations with respect to the foregoing claims and the purchases and sales of the machinery and other material were conducted by persons who were officers of the taxpayer and also officers of Supply, Bethlehem Steel Company, and Bethlehem Steel Corporation. These persons did not receive any compensation from the taxpayer during 1946 and 1947 and were compensated by one or more of the other companies. (R. 6a–7a.)

No entries of receipts or of disbursements were made on the taxpayer's books in connection with the settlement of the foregoing claims or in connection with the purchases and sales during the years 1946 and 1947 and all receipts or payments with respect thereto were or will be realized or made by Supply. A former employee of the taxpayer commenced an action in June, 1946, for alleged unpaid compensation in the amount of $219,000. The taxpayer filed an answer and took other action in that suit until November 1, 1948, when it was dismissed following the death of the plaintiff. The expenses of the litigation were borne partly by Supply and partly by former stockholders of the taxpayer from whom the Bethlehem Steel Company had purchased the taxpayer's stock. (R. 7a.)

The net proceeds of the sale of the taxpayer's properties were credited to the taxpayer in the inter-

company bank account maintained by subsidiary companies of Bethlehem Steel Corporation. No formal action to dissolve the taxpayer was ever taken by its board of directors or sole stockholder, and annual meetings of both were held during 1946 and 1947 for the purpose of electing directors and officers. The balance sheets of the taxpayer at the close of business on January 2, 1946, on December 31, 1946, and on December 31, 1947, were identical, consisting solely of accounts receivable in the intercompany bank account as assets and capital stock, paid-in surplus, and earned surplus in the capital accounts. (R. 7a–8a.)

The taxpayer acquired four sections of a dry dock in 1948 for approximately $800,000 and in 1949 purchased another section. The taxpayer's dry-dock facilities represented an investment of approximately $1,500,000 at the time of the hearing, and it was in the business of renting the dry dock. (R. 8a.)

In its excess-profits tax return for 1944, petitioner sought to carry-back an unused excess-profits credit for 1946 in the amount of $74,909.27. The Commissioner disallowed the attempted carry-back and determined a deficiency of $64,047.43. (R. 3a.) The Tax Court sustained the Commissioner's determination (R. 11a), and the Court of Appeals unanimously affirmed (Pet. Ex. B).

ARGUMENT

This case presents a narrow factual issue which does not merit review by this Court. Contrary to the assertion of the taxpayer, the case does not involve any questions of general importance. The decision

below is clearly correct and does not conflict with the decision of any other court of appeals.

1. Under the World War II excess-profits tax law, as set forth in Section 710 *et seq.* of the Internal Revenue Code of 1939[2] (Appendix, *infra*, pp. 15–17), normal profits are excluded from excess profits by means of an excess-profits credit, determined on the basis of invested capital or net income for a base period. This credit, if unused in the taxable year, could under certain circumstances be carried back for two years prior to the tax year. When the excess-profits tax was repealed as of December 31, 1945, the two-year carry-back provision was retained for a year beyond repeal in order "to be sure that business has the opportunity to apply reconversion expenditures to reduce wartime taxes." S. Rep. No. 655, 79th Cong., 1st Sess., p. 19. Thus, the unused excess-profits credit for 1946 could be carried back to 1944 and 1945.[3]

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[2] This law was added to the Internal Revenue Code of 1939 as Section 710 *et seq.* by Section 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974, applicable to taxable years beginning after December 31, 1939. References to "Code" or "Internal Revenue Code" are to the Internal Revenue Code of 1939 unless otherwise noted.

[3] Section 122 of the Revenue Act of 1945, c. 453, 59 Stat. 556, effective as of January 1, 1946. In this connection, Section 122 provides in part:

"SEC. 122. REPEAL OF EXCESS PROFITS TAX IN 1946.

"(a) *In General.*—The provisions of subchapter E of chapter 2 shall not apply to any taxable year beginning after December 31, 1945.

"(b) *Carry-backs From Years After 1945, Etc.*—Despite the provisions of subsection (a) of this section the provisions of subchapter E of Chapter 2 shall remain in force for the purposes of the determination of the taxes imposed by such subchapter for taxable years beginning before January 1, 1946, such determina-

The taxpayer corporation in the instant case was held not entitled to an unused excess-profits credit carry-back for 1946 when it had, as of the beginning of business on January 1, 1946, completely ceased its business operations.[4] The position of the Commissioner, as approved by both the Tax Court and the Court of Appeals for the Third Circuit, was that the taxpayer in the year 1946 was a mere corporate shell with no substance, and as such was not entitled to the relief provisions of the carry-back. This result is in harmony with the general rule that a corporation without a business purpose does not have to be treated as a corporation for tax purposes, and that the Commissioner may look through form to substance in order to protect the revenue. *Gregory* v. *Helvering*, 293 U. S. 465; *Higgins* v. *Smith*, 308 U. S. 473; *Commissioner* v. *National Carbide Corp.*, 167 F. 2d 304 (C. A. 2d), affirmed, 336 U. S. 422.

Whether a corporation is dissolved, *de facto* or *de jure*, presents a question of fact which must be considered in the light of the record of each particular case. In this case, the taxpayer sold all of its assets

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tion to be made as if subsection (a) had not been enacted but with the application of the amendments made by subsection (c) of this section and section 131 of this Act."

* * * * *

Subsection (c) of Section 122 amended Section 710 (c) of the Internal Revenue Code of 1939 so as to provide that there shall be no unused excess profits credit for a taxable year beginning after December 31, 1946.

[4] The Tax Court found that the taxpayer, at the beginning of 1946, had disposed of the assets essential to the continued operation of the business which it had conducted with those or similar assets in 1944 (R. 9a–10a); and that the business was no longer operated by the taxpayer (R. 10a).

to the Supply Company, a fellow subsidiary of Bethlehem Steel Corporation, the purchaser assuming the taxpayer's liabilities and obligations. (R. 4a–5a.) The net result of the sale was that the taxpayer divested itself of any and all business activity and became a corporation with one asset, namely, a credit in an intercompany bank account maintained in the name of subsidiary companies of Bethlehem Steel Corporation. (R. 7a.) Thus, at the beginning of 1946, the taxpayer was completely liquid, with its one asset, the bank balance, in the complete control of its sole stockholder, Bethlehem Steel Corporation. A transfer of this asset to the sole stockholder would have required no more than a simple bookkeeping entry.

The contention of the taxpayer that it was in existence in 1946 for a proper business purpose (Pet. 9–12) does not square with the findings of the Tax Court.[5]

[5] In this respect, the second question which the taxpayer presents (Pet. 2) inaccurately states that the Tax Court made a finding of fact "that the petitioner remained in existence in 1946 for a proper business purpose." A reading of the opinion of the Tax Court (R. 3a–10a) shows not only that such a finding was not made, but that on the contrary it was found (R. 9a–10a) that "The petitioner, at the beginning of 1946, disposed of the assets essential to the continued operation of the business which it had conducted with those or similar assets in 1944" and that "the business was thus transferred to another and no longer operated by the petitioner." The Tax Court found no more than that the taxpayer remained in technical legal existence. It did not find the taxpayer to be in existence for any business purpose. On the facts as found by the Tax Court, the Court of Appeals was clearly correct in holding that the taxpayer was *de facto* dissolved, and the fact that the Tax Court did not use the precise words "*de facto* dissolved" in nowise changes the correctness of the holding of the Court of Appeals.

As the Tax Court concluded, the taxpayer after January 1, 1946, "ceased to operate a business but remained in existence to cooperate with the purchaser so that the latter might derive the benefit of certain contracts and claims that were unassignable." (R. 3a.) While the taxpayer's name was used to consummate certain clean-up activities arising out of the transfer of the assets, these activities were for the benefit of the purchaser and were in no sense income-producing activities of the taxpayer. The persons who handled this clean-up work in the taxpayer's name were in the employ of the purchaser and other Bethlehem companies and they received their pay from those companies and not from the taxpayer. (R. 6a–7a.) That any so-called activities of the taxpayer in 1946 were actually activities of the purchaser Supply is evident from the fact that for over two years the taxpayer's balance sheet remained exactly the same as it was on January 2, 1946. (R. 7a–8a.)

Thus, during 1946, the taxpayer was a corporation in name only, without corporate substance and serving no real corporate purpose. The charter was merely kept in storage for possible future use in the Bethlehem Steel Corporation family of corporations. Under those circumstances, the taxpayer was correctly treated as a *de facto* dissolved corporation for the purpose of the two-year carry-back provision, and it would flout the intention of Congress to hold otherwise. The provision was originally designed for use only in cases where the credit was not needed in the tax year to offset normal earnings (S. Rep. No. 1631, 77th Cong., 2d Sess., pp. 51–52); and, as already pointed

out, the provision was retained for a year beyond the repeal of the excess-profits tax itself in order "to be sure that business has the opportunity to apply reconversion expenditures to reduce wartime taxes" (S. Rep. No. 655, 79th Cong., 1st Sess., p. 19). Where, as in the instant case, the taxpayer had ceased to operate, there is no adequate basis for extending the benefits of the provision to such a nonoperating corporation.[6]

2. The taxpayer contends (Pet. 5–6) that the decision below is in conflict with decisions of other courts of appeals which, it is claimed, held that the carry-back provision is "mandatory" (Pet. 6). *Diamond A Cattle Co.* v. *Commissioner* (C. A. 10th), decided May 17, 1956 (1956 C. C. H., par. 9629); *Wier Long Leaf Lumber Co.* v. *Commissioner*, 173 F. 2d 549 (C. A. 5th); *Bowman* v. *Glenn*, 84 F. Supp. 200 (W. D. Ky.), affirmed, *per curiam*, 184 F. 2d 670 (C. A. 6th). None of these decisions, however, held that the credit carry-back must be allowed where the taxpayer is *de facto* dissolved. Each is distinguishable on its particular facts.

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[6] The fact that the taxpayer, after two years of complete business inactivity, had life blown into it and is presently engaged in the drydock business, does not serve to make it any the less *de facto* liquidated during the year 1946 when all of its assets had been reduced to an inter-company bank account and it had discontinued operating. It was during that year no more than a corporate shell. The subsequent revitalization of the taxpayer serves, as a matter of fact, to point out the reason that there was no *de jure* dissolution at the time of the *de facto* dissolution. At that time, the charter was stored away, to be subsequently used by the parent for any one of the multiple reasons for which the Bethlehem Steel Corporation would form a corporation.

In the *Diamond A Cattle Co.* case, *supra*, the taxpayer corporation until mid-1945 was engaged in extensive livestock business and some farming. It began to liquidate in August, 1945, by a transfer of all its assets to its sole shareholder. For the remainder of the year, its business consisted of paying a few debts and in winding up its affairs. Not finding any factual basis for determining the taxpayer *de facto* dissolved for the few months remaining in 1945, the Tenth Circuit held that the taxpayer was entitled to carry-back its unused excess-profits credit for 1945, the year in which it had been operating, to prior years.

Likewise, the Fifth Circuit in the *Wier* case, *supra*, came to a result completely in accord with the case at bar. In *Wier*, the question was whether a taxpayer which began liquidation in 1942 and continued in liquidation during 1943 and 1944 was entitled to the benefit of the unused excess-profits credit carry-back for 1943 and 1944. The court stated unequivocally that if it appeared that the corporation was a corporation in name and semblance only, without corporate substance and serving no real corporate purpose, it must, though not formally dissolved, be treated as dissolved *de facto*. Applying this standard, which is the same one adopted by the Third Circuit for its decision in the instant case, the Fifth Circuit allowed the carry-back for the year 1943 and disallowed a carry-back for 1944. It held that in 1943 the corporation (p. 552) "was still in form and in fact a corporation, still carrying on, in winding up, the business for which it was incorporated, still mak-

ing some, though small, profits, still engaged in necessary and orderly liquidation." As to the year 1944, however, the court held that the liquidation had progressed to the point where there was no longer any valid reason for delaying dissolution, and the corporation, although not dissolved *de jure*, was to be regarded as *de facto* dissolved.

The District Court in *Bowman* v. *Glenn*, *supra*, citing the *Wier* case, also looked to the actualities of the situation, and found that there were no facts presented in that case regarding the liquidation of a corporation to indicate that it was needlessly prolonged or purposely extended.

All of the cases cited by the taxpayer tend to support the position of the Commissioner that the mere fact that a corporation is not *de jure* dissolved is not in itself sufficient to allow to the corporation the benefits of the unused excess-profits credit carry-back under Section 710 (c) (3) (A). Rather, the courts will in each instance look to the realities of the situation, to the nature and extent of the activities of the corporation, and where a corporation remains a mere shell of no substance, as in this case, the benefits of the credit will be denied. See also *A B C Brewing Corp.* v. *Commissioner*, 224 F. 2d 483, 490 (C. A. 9).

CONCLUSION

The decision below is correct, there is no conflict in decisions, and no other reason appears which would warrant review. Accordingly, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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AUGUST 1956.

APPENDIX

Internal Revenue Code of 1939:

SEC. 710 [as added by Sec. 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974]. IMPOSITION OF TAX.

(a) [as amended by Sec. 201 (a) of the Revenue Act of 1941, c. 412, 55 Stat. 687; Sec. 202 of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Imposition.*—

(1) *General rule.*—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

* * * * *

(b) *Definition of Adjusted Excess Profits Net Income.*—As used in this section, the term "adjusted excess profits net income" in the case of any taxable year means the excess profits net income (as defined in section 711) minus the sum of:

* * * * *

(2) *Excess profits credit.*—The amount of the excess profits credit allowed under section 712; and

(3) [as amended by Sec. 2 (a) of the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, and Sec. 204 (a) of the Revenue Act of 1942, *supra*] *Unused excess profits credit.*—The amount of the unused excess profits credit adjustment for the taxable year, computed in accordance with subsection (c).

(c) [as added by Sec. 2 (b) of the Excess Profits Tax Amendments of 1941, *supra*, and amended by Sec. 204 (b) of the Revenue Act of

1942, *supra*, and by Sec. 122 (c) of the Revenue Act of 1945, c. 453, 59 Stat. 556] *Unused Excess Profits Credit Adjustment.*—

(1) *Computation of unused excess profits credit adjustment.*—The unused excess profits credit adjustment for any taxable year shall be the aggregate of the unused excess profits credit carry-overs and unused excess profits credit carry-backs to such taxable year.

(2) *Definition of unused excess profits credit.*—The term "unused excess profits credit" means the excess, if any, of the excess profits credit for any taxable year beginning after December 31, 1939, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year. For such purpose the excess profits credit and the excess profits net income for any taxable year beginning in 1940 shall be computed under the law applicable to taxable years beginning in 1941. The unused excess profits credit for a taxable year of less than twelve months shall be an amount which is such part of the unused excess profits credit determined under the first sentence of this paragraph as the number of days in the taxable year is of the number of days in the twelve months ending with the close of the taxable year. There shall be no unused excess profits credit for a taxable year beginning after December 31, 1946. The unused excess profits credit for a taxable year beginning in 1946 and ending in 1947 shall be an amount which is such part of the unused excess profits credit determined under the preceding provisions of this paragraph as the number of days in such taxable year prior to January 1, 1947, is of the total number of days in such taxable year.

(3) *Amount of unused excess profits credit carry-back and carry-over.*—

(A) *Unused Excess Profits Credit Carry-Back.*—If for any taxable year beginning after

December 31, 1941, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such unused excess profits credit over the adjusted excess profits net income for the second preceding taxable year computed for such taxable year (i) by determining the unused excess profits credit adjustment without regard to such unused excess profits credit, and (ii) without the deduction of the specific exemption provided in subsection (b) (1).

* * * * *

(26 U. S. C. 1952 ed., Sec. 710.)

Treasury Regulations 112, promulgated under the Internal Revenue Code of 1939:

SEC. 35.710–1. *Scope of Tax.*—The excess profits tax is imposed upon the adjusted excess profits net income of every corporation, both domestic and foreign, for each income-tax taxable year beginning after December 31, 1939, except certain corporations which are exempt. (See section 727.) * * *

SEC. 35.710–2 [as amended by T. D. 5478, 1945 Cum. Bull. 262]. *Measure of Tax.* The adjusted excess profits net income upon which is based the excess profits tax for a taxable year is determined by deducting from the excess profits net income (determined under the provisions of section 711 applicable to such year) the sum of:

(a) The specific exemption applicable to such taxable year, as provided in section 710 (b) (1). See section 35.710–1.

(b) The excess profits credit allowed by section 712, and

(c) The unused excess profits credit adjustment (as defined in section 710 (c) (1)) con-

sisting of the aggregate of the unused excess profits credit carry-overs from each of the two preceding excess profits tax taxable years and the excess profits credit carry-backs from each of the two succeeding excess profits tax taxable years, computed as provided in section 710 (c).

* * * * *

SEC. 35.710-3 [as amended by T. D. 5386, 1944 Cum. Bull. 374; T. D. 5478, *supra;* and T. D. 5514, 1946-1 Cum. Bull. 173]: *Unused Excess Profits Credit Adjustment.*—(a) *Unused excess profits credit.*—The unused excess profits credit for any taxable year beginning after December 31, 1939, is the excess of the excess profits credit for the taxable year over the excess profits credit income, if any, for such taxable year. In the case of a taxpayer entitled to use the excess profits credit based on income or the excess profits credit based on invested capital, the credit which results in the larger unused excess profits credit is used. The excess profits net income is computed on the basis of the excess profits credit so used. * * *

* * * * *

A corporation may have an unused excess profits credit for a taxable year beginning in 1946, which may be carried back to the two preceding taxable years, even though no excess profits tax is imposed for such taxable year. The unused excess profits credit for a taxable year beginning in 1946 is to be computed in the same manner as though an excess profits tax were imposed for such taxable year. * * * There will be no unused excess profits credit for a taxable year beginning after December 31, 1946.

(b) *Unused excess profits credit adjustments.*—The unused excess profits credit adjustment is the aggregate of the portions of the unused excess profits credits for the two pre-

ceding and two succeeding taxable years which are treated under section 710 (c) (3) as unused excess profits credit carry-overs and unused excess profits credit carry-backs to the taxable year. Under the provisions of section 710 (c) (3) the unused excess profits credit for any taxable year beginning on or after January 1, 1942, is carried back to each of the two preceding taxable years (not considering as a preceding taxable year any taxable year beginning before January 1, 1941) and forms part of the unused excess profits credit adjustment for such preceding taxable year. There will be no unused excess profits credit carry-back from any taxable year beginning after December 31, 1946. The unused excess profits credit for any taxable year beginning after December 31, 1939, to the extent it is not used as a carry-back, is carried forward to the two succeeding taxable years and forms part of the unused excess profits credit adjustment for such of those succeeding taxable years as begin after December 31, 1940. The amount which is carried back or carried forward is limited in the case of each such preceding or succeeding taxable year to the portion of the unused excess profits credit which was not applied against excess profits net income (either as part of the excess profits credit carry-over in the case of a taxable year beginning in 1940 or as part of the unused excess profits credit adjustment in the case of a taxable year beginning after December 31, 1940) in determining the adjusted excess profits net income for the taxable years, if any, before such preceding or succeeding taxable year. The amount of the unused excess profits credit which was so applied is determined as follows: The adjusted excess profits net income is computed for each such taxable year without the specific exemption allowed by section 710 (b) (1) and without credit of any carry-over or carry-back from the taxable year in which such unused

excess profits credit arose or from any taxable year subsequent thereto. The unused excess profits credit, which is a carry-over or a carry-back to such taxable year, is considered to have been applied against the amount so computed. * * * The entire unused excess profits credit for any taxable year beginning after December 31, 1941, is carried back to the second preceding taxable year if such taxable year began after December 31, 1940. * * * If the second preceding taxable year began after December 31, 1940, the unused excess profits credit is carried back to the first preceding taxable year to the extent it exceeds the adjusted excess profits net income for the second preceding taxable year, such adjusted excess profits net income being computed without credit of the applicable specific exemption and without credit of any carry-back from the taxable year in which the unused excess profits credit arose. The unused excess profits credit is carried over to the first succeeding taxable year to the extent that it exceeds the aggregate of the adjusted excess profits net incomes for the two preceding taxable years (computed for each such taxable year without credit of the applicable specific exemption and without credit of any carry-back from the taxable year in which such unused excess-profits credit arose or of any carry-back from a taxable year subsequent thereto), not considering as a preceding taxable year any taxable year beginning prior to January 1, 1941. * * *

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